

City Manager's Budget Update Message

November 15, 2001

Mayor, City Council and Citizens of Cincinnati:

I am transmitting to the City Council my 2002 Budget Update which includes my recommended changes to the 2002 Approved Budget, the second year of the 2001/2002 Biennial Budget. Provided herein are the 2002 Operating Budget Update Report, the 2002 Capital Budget Update Report and the 2002 Consolidated Plan Budget Update Report. Table 1 summarizes the 2002 Budget Update. Overall, my recommended Budget Update is 1.1%, or \$11.5 million, less than the 2002 Approved Budget.

This Budget Update is different from previous updates because the number of recommended budget changes is greater than usual. Most of these changes have to do with the lower expected revenues for the General Fund and other City funds that depend on the City's Income Tax. These changes are highlighted herein and are detailed in the accompanying documents.

I reported in June 2001 that we expected a \$17.7 million deficit for the General Fund in 2002 unless budget-balancing actions were taken. We have been able to balance the 2002 budget and provide a small \$2.1 million year-end carry-over balance. This \$19.8 million change was accomplished by the following actions: \$3.6 million in 2002 operating budget expenditure reductions; \$17.6 million in 2002 capital budget decreases, including prior approved project cancellations, project deferrals to future years, and shifting projects to other funds; and using \$3.9 million in 2001 additional carryover funds. These additional resources are offset by a \$5.3 million reduction in 2002 estimated revenue.

Even though the Budget Update includes budget cuts, essential City services and projects are maintained. Basic City services will continue to be provided such as police and fire protection, refuse collection, water and sewer services, primary health clinics, building inspections, recreation programs, and parks. Ongoing projects will continue such as rehabilitating 100 lane miles of streets, City facility maintenance, and technology improvements. A few areas are increased in the budget such as 30 additional police recruits, staff support for emergency preparedness, an additional paramedic engine company, and increased downtown parking.

The Operating Budget Update is increased by 0.5%, or \$3.5 million, over the 2002 Approved Budget. The General Fund component is reduced by 0.6%, or \$2 million, to adjust for decreasing revenues. It is noteworthy that the General Fund has a \$2 million reduction even though employee benefits have increased by \$2 million, primarily for employee health care. The Restricted Funds component is increased by 1.4%, or \$5.5 million, primarily due to increases in the Bond Retirement Fund and the Metropolitan Sewer District (MSD) Fund which are offset by reductions in the Transit, Infrastructure, Water Works and Convention Center Funds.

Table 1: 2002 All Funds Budget Summary

(In \$ Millions)	2001 Approved Budget	2002 Approved Budget	2002 Budget Update	% Change 2002 Update/ 2001 App.	% Change 2002 Update/ 2002 App.
Operating Budget					
General Fund	\$308.1	\$316.9	\$314.9	2.2%	-0.6%
Restricted Funds	377.2	387.5	393.0	4.2%	1.4%
Subtotal	\$685.3	\$704.4	\$707.9	3.3%	0.5%
Capital Budget					
General Capital	\$77.9	\$137.9	\$78.1	0.3%	-43.4%
Restricted Funds	146.1	137.2	180.8	23.8%	31.8%
Subtotal	\$224.0	\$275.1	\$258.9	15.6%	-5.9%
Consolidated Plan Budget	\$28.2	\$25.5	\$26.7	-5.3%	4.7%
Total Budget	\$937.5	\$1,005	\$993.5	6.0%	-1.1%

The Capital Budget Update is decreased by 5.9%, or \$16.2 million, from the Approved Budget. The General Capital component is reduced by 43.4%, or \$59.8 million, to reflect the recommended shift in the Convention Center expansion to 2003 and the recommended shift of several projects to restricted funds to avoid further cuts in the General Fund. The Restricted Funds Capital Budget is increased by 31.8%, or \$43.6 million, to reflect the increase in Metropolitan Sewer District capital projects and the expansion of parking facilities downtown.

The Consolidated Plan Budget Update is increased by 4.7%, or \$1.2 million, from the 2002 Approved Budget level, but this reflects a continuation of the 2001 Approved Budget annual grant amounts, program income, and amounts carried over from prior years.

GENERAL FUND CONDITION

Revenue and the Economy

The Approved 2001/2002 Biennial Budget shows 2001 General Fund revenue to be \$316.9 million and 2002 General Fund revenue to be \$324 million. The current estimated General Fund revenue for 2001 is \$308.5 million and the 2002 General Fund revenue estimate is \$309 million. For the 2001/2002 biennium the revenue decrease from estimate is \$23.4 million, or 3.7%. The decrease in 2001 from the original budget is \$8.4 million and the decrease in 2002 from the original budget is \$15 million.

It is currently estimated that the 2001 General Fund revenue will grow by only 2.4%, or \$7.3 million, over the 2000 actual revenue amount. The primary reason for the lower revenue estimate for 2001 is the poor performance of the Income Tax. Income Tax is expected to be \$188.1 million for 2001, 2.75% more than 2000. The original 2001 budget estimate for Income Tax revenue was \$199.6 million, which is \$11.5 million more than the estimated 2001 amount.

Table 2: General Fund Revenues (in \$000's)

	2000	2001	2001	2002	2002	Percent Change	
	Actual	Budget	Estimate	Budget	Update	Update vs	Update vs
						2001 Est.	2002 Bud.
Income Tax	183,035	199,563	188,068	204,066	191,830	2.0%	-6.0%
Property Tax	29,719	28,660	28,660	28,660	28,660	0.0%	0.0%
Estate Tax	14,689	15,750	19,500	16,300	17,100	-12.3%	4.9%
Local Government Fund	30,949	32,035	32,157	33,000	32,157	0.0%	-2.6%
Investments	11,579	11,700	13,200	12,050	10,100	-23.5%	-16.2%
Other Revenues	31,191	29,193	26,910	29,950	29,132	8.3%	-2.7%
Total Revenue	301,162	316,901	308,495	324,026	308,979	0.2%	-4.6%

For 2002, General Fund revenue is estimated to be \$309 million, which is a scant 0.2% increase over the 2001 estimate. While we expect Income Tax revenue to grow by 2%, or \$3.8 million, this will be offset by an estimated \$3.1 million decrease in Investments revenue because of declining interest rates; an estimated \$2.4 million reduction in Estate Tax revenue because we do not expect the 2001 receipts to be sustained in 2002; and by increases in other revenue of \$2.2 million. The original 2002 budget estimate for Income Tax revenue was \$204.1 million, which is \$12.2 million more than the estimated 2002 amount.

The fiscal health of the City is highly dependent upon the performance of the Income Tax. Income Tax revenue not only makes up 62% of the General Fund but also provides revenue for infrastructure, capital improvements, and public transit. The sources of Income Tax revenue are business profits and employee wages. The local and national reported declines in business profits and payroll, and the increase in unemployment do not bode well for the City's Income Tax revenue. The consensus among economists is that the economy is in a recession now, but it will rebound in the second half of 2002. Blue Chip Economic Indicators (October, 2001), which surveys 50 economists monthly, shows the national economy growing by only 1.5% in 2002 as measured by the Gross Domestic Product. DRI/WEFA (formerly Standard & Poor's DRI) estimates national economic growth at 1.3% for next year (U.S. Economic Review, October, 2001). These recession scenarios support the Income Tax revenue slow growth estimates of 2.75% in 2001 and 2% in 2002. In fact, we have consulted with economists at DRI/WEFA, and they support our 2002 Income Tax revenue growth estimate.

The tragedies of September 11, 2001, the war on terrorism, and new threats posed by weapons of mass destruction all increase uncertainty and make predicting economic performance nationally or locally a difficult exercise. We will monitor Income Tax and other revenue performance very closely and report to the City Council promptly if actual revenues diverge from the estimates. Our intention is to engage an economic forecast firm in the spring of 2002 to assist in developing the next six-year forecast.

Fund Balance Estimates

Table 3 shows the impact of the sharp decline in revenues on the City's budget in 2001, 2002, and 2003. Carryover balances decline sharply in 2002 and 2003. The small surplus in 2002 becomes a large deficit of \$27 million in 2003. The deficit is the result of a small carryover from 2002, decreased revenue for 2003, and increased planned capital transfers for 2003. Obviously, additional expenditure cuts will have to be made for 2003 unless revenues greatly improve.

The \$2.1 million carryover balance in 2002 is very low compared to recent annual balances. It is only 0.6% of 2002 revenue. If, for example, 2002 Income Tax revenue increases by only 1% instead of the estimated 2%, the carryover balance at the end of 2002 would be nearly zero. Because the margin of carryover is so narrow, the City may have to tap the Working Capital Reserve or "rainy day" fund in 2002 to avoid a deficit. This reserve, which was established by City Council policy, maintains a balance of not less than 5% or more than 8% of general operating revenue to meet emergency and catastrophic needs. Using the reserve is not without negative consequences. Bond rating agencies have looked favorably at the Reserve and tapping it for operating needs may have an adverse impact on the City's bond rating.

Table 3: 2001 – 2003 General Fund Fund Balance Summary

	2001 Budget	2001 Estimate	2002 Budget	2002 Update	2003 Projected
Operating Revenue	316,901	308,495	324,026	308,979	317,012
Operating Expenditures:					
City Operations	303,076	303,076	311,946	309,311	318,912
Payment to Public Schools	5,000	5,000	5,000	5,000	5,000
75 Additional Police Officers				583	4,257
Total Operating Expenditures	308,076	308,076	316,946	314,894	328,169
Operating Expenditure Savings	-4,548	-5,223	-4,679	-4,648	-4,784
Capital Transfers:					
Debt Service and Neighborhood Investment Program	22,753	12,174	17,657	6,052	22,692 *
Surplus (Deficit) After Transfers	-9,380	-6,532	-5,898	-7,319	-29,065
Prior Year Carryover Balance	15,917	15,917	6,537	9,385	2,066
Surplus (Deficit) After Transfers	-9,380	-6,532	-5,898	-7,319	-29,065
Ending Year Carryover Balance	6,537	9,385	639	2,066	-26,999
*Includes a \$6 million transfer for the Fort Washington Way project that was deferred in 2001 and 2002					

Recommendations to Balance the Budget

Without significant expenditure reductions, the City will face a large deficit in 2003. The addition of 75 police officers will cost \$4.3 million in 2003 and the full implementation ongoing cost will be more than \$6 million annually. I recommend that City Council reconsider its decision to add these police officers. A more detailed explanation in support of this recommendation follows on the next page.

In order to minimize future layoffs, I also recommend that the selective hiring freeze be continued in 2002. All but the most critical vacancies should be eliminated. In addition, the capital transfers planned for 2003 must be significantly reduced.

I also recommend that the Mayor, Members of City Council, and the City Administration begin early in 2002 to set expenditure priorities for the 2003/2004 Biennial Budget.

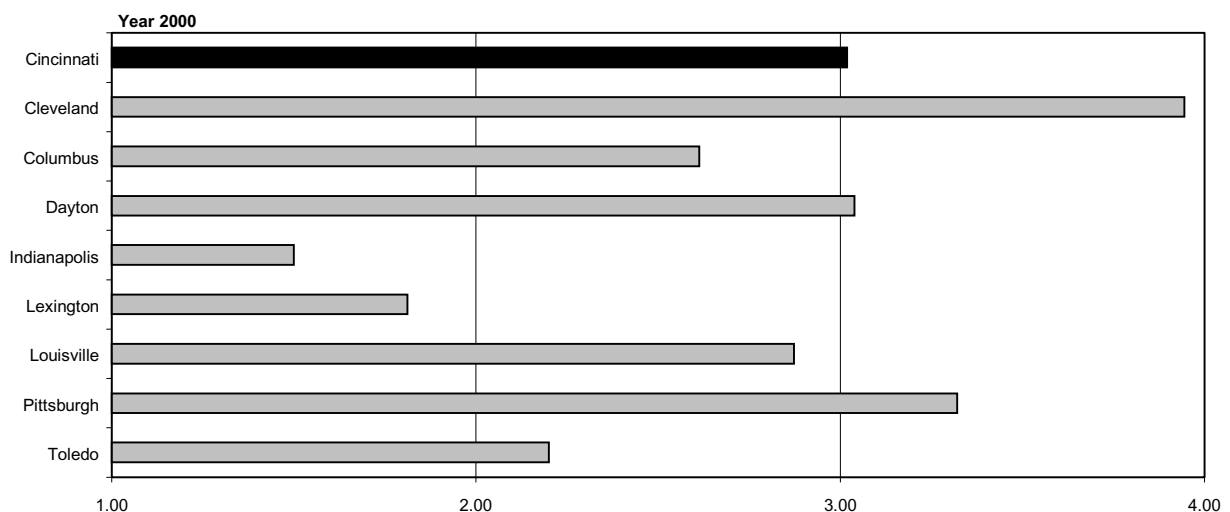
SIGNIFICANT BUDGET ISSUES

General Fund Significant Increases

30 Police Recruits (\$582,960). A motion adopted by the City Council on October 3 calls for increasing the authorized strength of the Police Division by 40 police officers in 2002 and 35 police officers in 2003. After discussions with the Safety Director and Police Chief, we have concluded that adding 40 officers in 2002 will not be feasible largely due to a shortage of candidates in the available applicant pool. Therefore, this budget contains funding for 30 additional police recruits which will be hired in the second recruit class scheduled to begin in early August. These recruits will become police officers and be added to the authorized strength of the Police Division in January 2003. To achieve the Council's goal of 75, 30 recruits will be added to the January 2003 class and 15 to the July 2003 class.

As noted, I recommend that the City Council reconsider its decision to add 75 police officers because the City cannot afford them and because the current authorized strength of 1,000 is sufficient. The current size of the Police Division's sworn force compares very favorably

Table 4: Sworn Police Officers per 1,000 Population



with other cities across the country. The most recent comparison conducted by the International City/County Management Association (ICMA) shows that Cincinnati ranks fifth out of twenty-nine cities and counties surveyed in the number of sworn officers per 1000 population. Of the comparable cities in our region, only Cleveland and Pittsburgh have a higher ratio of sworn officers per population. Our ratio is higher than cities such as Columbus, Toledo, Lexington, Louisville and Indianapolis.

Crime statistics indicate criminal activity has declined in Cincinnati over the past several years. Cincinnati experienced a 34% decline in major crimes such as homicide, rape, robbery, aggravated assault, theft and arson between 1991 and 2000. The drop in violent crime (homicide, rape, robbery and assault) was 48% over the same period. The civil unrest and the violence that occurred in certain areas of the City in its aftermath will certainly reverse the downward trend in crime for 2001. However, it is too soon to know whether the recent increase in criminal activity constitutes a trend. In addition, there is little evidence to support the notion that adding 75 officers will reduce the types of violent crime we have seen recently. I recommend that the Mayor and the City Council carefully weigh the benefits of adding the additional 75 officers against service reductions in areas such as health, recreation, human services, and neighborhood investment that will be needed to balance future budgets.

Legal Expert Services (\$705,000). The Law Department will receive additional funding to cover the costs of the ongoing U.S. Justice Department review, racial profiling litigation, police arbitration cases and other expert services.

Employee Health Care Costs (\$3.5 million). The dramatic increase in health insurance costs is a nationwide problem. This additional funding will bring the amount budgeted in the General Fund for employee health care to \$15.7 million, or 29% more than the 2002 Approved Budget level. Fortunately, rebates from the State associated with positive workers compensation experience will offset \$2.3 million of this increase. The City will spend \$23.2 million in the General and Restricted Funds in 2002 for employee health care.

Weapons of Mass Destruction/Emergency Preparedness (\$56,850). The Fire Division will receive additional funding so that a Fire Lieutenant position can be dedicated full time to activities related to dealing with weapons of mass destruction and emergency preparedness.

Engine Company Conversion (\$67,950). Additional funding is recommended for the conversion of an engine company to a paramedic engine company at Firehouse 49 in Madisonville. This will improve response time in the surrounding areas.

General Fund Significant Reductions:

In order to achieve the necessary reductions in the General Fund, most departmental budgets were reduced approximately 5% from the Approved 2002 level. Reductions of this magnitude cannot be made without some effect on services. Examples of these service reductions include:

Health and Human Services

Nursing Home Licensing (\$190,130). Once again I am recommending that the City Council not require the Health Department to perform a service that the State is required to perform.

School Health Nursing Program (\$289,720). This reduction includes 4.4 nurse FTE and 2 support FTE leaving 19.7 FTE nurses. However, a portion of the school nursing program is funded through the Health Department's agreement with the Empowerment Zone Corporation. EZ funds will increase nurse FTE from 4.6 to 6.6 and add 1 support FTE. The net decrease in nurse FTE is 2.4 for the School Health Nursing Program.

Elimination of the Office of Consumer Services (\$145,320). While this service has been valuable in assisting citizens with problems, it is not an essential municipal service. The two employees in this office will be placed in vacant positions elsewhere within the City government.

Human Services Policy (\$243,000). As a result of the significantly lower revenue estimate, the Human Services Policy amount is \$225,800 lower than the level assumed in the Approved Budget. However, in keeping with my goal to reduce as many budgets as possible by 5% from the 2002 Approved level, I am recommending an additional reduction of \$17,310. Other organizations that receive funding from the City that are not part of the Human Services Policy have also been reduced by 5%.

Arts Policy (\$22,680). As with the Human Services Policy, most of this reduction relates to the lower projected revenues. However, \$1,610 represents the amount needed to achieve a 5% reduction.

Hazard Abatement (\$221,160). The Department of Buildings and Inspections' General Operating Fund allocation for hazard abatement has been eliminated. The Department has \$527,500 in CDBG funds for 2002 and \$58,000 in General Capital funds in 2002 to continue this important program. Additionally, \$600,000 in unspent General Capital funds that was appropriated in 2000 for a large building demolition is available to keep the City's hazard abatement program at the 2001 funding level for the next two years.

Parks

Nature Education Program (\$250,200). The total budget for the Nature Education and Center Program in the Parks Department is approximately \$500,000, with 70% coming from the General Fund. Nature education services are currently provided during weekend programs, school field trips, day camps, after school programs, and special events. I recommend that the remaining funds be utilized for school field trips and after-school programs.

Recreation

Close 6 Pools (\$87,420). The following Department of Recreation pools are recommended for closure: Bramble Shallow Water, Owls Nest Shallow Water, Mt. Airy Shallow Water, Laurel Shallow Water, Rapid Run Shallow Water, and Rakestraw Deep Water. These pools were selected based on factors such as high maintenance costs, low attendance, and proximity to other pools.

Other City Department Reductions (\$1.7 million). Most departmental budgets are reduced 4 to 5 percent from the 2002 Approved Budget. These reductions result from eliminating vacant positions and cutting back on purchases of various supplies and equipment.

Non-Departmental

Reserve for Contingencies (\$500,000). This line item is reduced by 50% from the 2002 Approved Budget level. While no earmarks for this reserve have been identified, the City could incur additional costs related to improving security at public facilities and implementing some of the recommendations of the final Justice Department report on the Police Division.

Transfers to the Capital Budget

Neighborhood Investment Program (\$4 million). As stated earlier, the decrease in Income Tax revenues has significant implications for the City Council plan to transfer extra operating revenue to the capital budget to enhance a number of neighborhood-based initiatives. The major reductions include the following:

- Reducing the Street Rehabilitation target from 115 to 100 miles (this is the actual goal established by the City Council) saving \$2 million,
- Reducing the allocation for the Neighborhood Market Rate Housing Program by \$1 million, and
- Eliminating the \$1 million extra allocation to Neighborhood Business Districts which was part of the City Council's policy directive in 2001.

Other Capital Transfer Reductions (\$7.6 million). The following recommendations further reduce the amount of operating revenue that will be transferred to the capital budget in 2002:

- Utilize \$2.9 million in capital funds from the 2001 capital sunset process to fund a portion of the Street Rehabilitation program,
- Shift \$2.5 million in debt service payments related to Convention Center expansion to 2003,
- Use \$2.2 million in savings in 2002 from the Postal Service's decision to cancel the construction of a new facility in Bond Hill.

Other Expenditure Items

Contract Out Street Sweeping. The Department of Public Services will issue a Request for Proposals to contract out the street sweeping function in the Central Business District and in Over-the-Rhine. If acceptable bids are received, we will compare the costs and quality of service of a private vendor with the street cleaning operations performed in other neighborhoods utilizing City staff. We continue to have problems citywide with availability of equipment and the frequency of the service.

Over-the-Rhine Cleanup. This contracted trash pickup program was funded with one-time CDBG funds in 2001 through April, 2002. To continue the program for the remainder of 2002, the cost would be \$388,000. Because of budget limitations this is not included in the

2002 Budget Update; however, if the final CDBG grant amount is higher than expected, this program should be the first priority.

Recommended Fee Increases

This budget contains two fee increases in the General Fund:

Vital Records (\$200,000). An increase of \$2 in the fee charged by the Health Department for providing vital records (birth and death certificates) is recommended. The increase to \$12 is in line with other large cities in Ohio.

Emergency Medical System (\$600,000). The fees that the Fire Division collects primarily for emergency medical service are recommended to be increased. The increased fees reflect the increase in federally-approved reimbursements. The City will continue its practice of not collecting from persons who do not have insurance and are not able to pay.

Restricted Funds Significant Issues - Convention Center

Detailed explanations of all of the changes in the Appropriated Restricted Funds are provided in the Operating Budget Summary. However, I want to alert the City Council regarding the serious condition of the Convention Center Fund. In 2002, expenses at the Cincinnati Convention Center are expected to outpace revenue, continuing a three-year trend. The fund balance for the facility will likely erode to zero by the end of 2002.

The management team at the Convention Center has carried out several cost-saving measures to reduce expenses, such as reducing contract labor hours and implementing an aggressive energy savings plan. However, it is clear that the Convention Center cannot be sustained as an operationally self-supporting facility without additional resources.

I recommend that the City Council increase the Transient Occupancy Tax from 1.5% to 3% for 2002. This increase will generate approximately \$1.2 million annually. Of this amount, I recommend that the Greater Cincinnati Convention and Visitor's Bureau receive approximately \$300,000 to use for incentives to attract conventions to Cincinnati. The Convention Center will receive approximately \$900,000 of the revenue from the tax increase, which can be used for operating expenses if needed. Funds not needed for the operation of the existing Center and marketing will be held in reserve to fund Center expansion. I recommend that the City Council take this action to increase the Transient Occupancy Tax to be effective in January, 2002.

Recommended Fee Increases

Water Works Fund (\$2,190,000). A 3% rate increase is recommended, consistent with the 2002 Approved Budget and previously presented to the City Council.

Metropolitan Sewer District (\$6,134,000). A 6% rate increase was included in the 2002 Approved Budget and is recommended for submission to the Hamilton County Commissioners for their decision.

Department of Recreation (\$146,600). The Recreation Commission is proposing to raise membership fees at community centers and pool fees. The increased fees will help support community center programs funded out of the Recreation Special Activities Fund.

CAPITAL BUDGET ISSUES

The 2002 Capital Update Budget is 5.9% below the 2002 Approved Budget primarily because of a decline in the General Capital Budget. The Convention Center Expansion Project is delayed another year and several projects that were to be funded through transfers from the General Operating Fund were either reduced or transferred to Restricted Funds. Some of the significant items that are in the Update Budget include:

\$29.2 million of Street Rehabilitation and Improvement Projects,

\$17.7 million for Downtown Development Projects,

\$18 million for new Downtown Parking Garages,

\$5.3 million for Housing Development Projects,

\$6.1 million for the Citywide Communications System Project,

\$0.7 million for Community Facilities Improvement: Art Museum, Music Hall and Museum Center (the latter added for 2002 only).

The 2002 Capital Budget Update Report provides detailed descriptions of these projects and all of the adjustments I am recommending to the Approved Capital Budget.

CONSOLIDATED PLAN ISSUES

My recommended Consolidated Plan Update Budget is 4.7% more than the 2002 Approved level. The Update budget reflects the City Council's desire to put greater emphasis on home ownership.

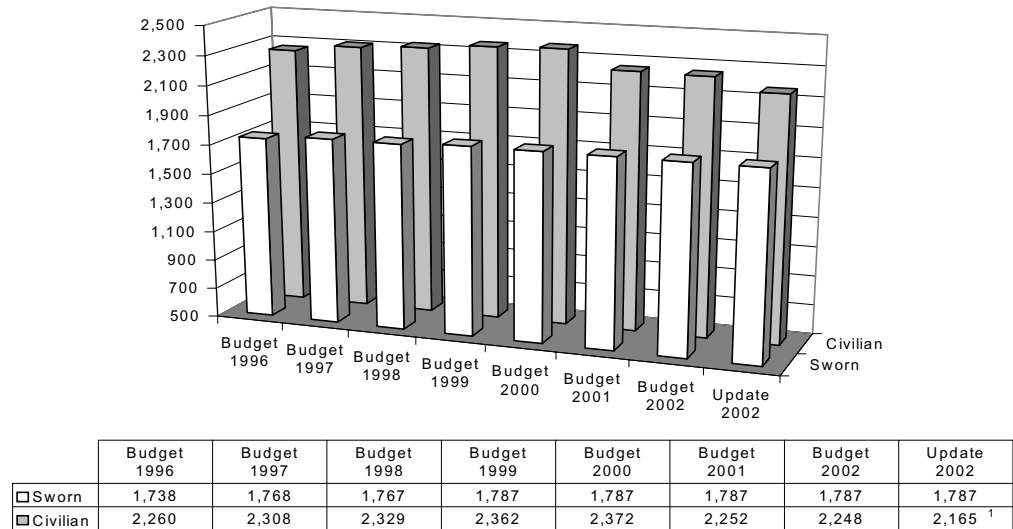
The 2002 Consolidated Plan Budget Update Report details my recommended changes for programs funded with Community Development Block Grant, HOME, Emergency Shelter Grants, and Housing Opportunities for Persons with AIDS federal dollars.

STAFFING

A total of 6,570.5 full-time equivalent positions (FTE) are recommended in the 2002 Operating Budget Update, a decrease of 39.5 FTE from the 2002 Approved Budget. This decrease is primarily due to the reduction of 5.2 FTE in the Finance Department, the net reduction of 9.0 FTE in the General Services Department after the transfer of the General Aviation Division to the Transportation and Engineering Department, the net reduction of 6.2 FTE in the Health Department, the net reduction of 6.8 FTE in the Parks Department, the

reduction of 5.0 non-sworn FTE in the Police Division, and a net reduction of 7.3 FTE in other departments. Descriptions of all FTE changes are included in the “2002 Staffing Plan” section of the 2002 Operating Budget Update Report.

Table 5: General Fund Sworn and Civilian Staffing Trend



¹ Includes an additional 26.8 FTE associated with the new Madisonville and College Hill recreation centers.

General Fund Staffing Trend

This budget reduces the number of full time equivalent (FTE) positions in the General Fund by a net of 82.4 from the 2000 Approved Budget. The General Fund net reduction reflects a citywide reduction of 109.2 FTE offset by the addition of 26.8 FTE in the Department of Recreation required for staffing new recreation centers in College Hill and Madisonville. While some of the General Fund positions were shifted to Restricted Funds in accordance with their functions, a net of 39.5 FTE have been eliminated citywide. Funding for thirty additional police recruits is included; however, the authorized sworn strength remains at 1,000 since the new recruits will not graduate until January of 2003. As shown in Table 5, the number of civilian FTE in the General Fund will be below the level of 1996.

I recommend that public hearings on the budget take place in December and that the City Council approve the budget by December 19, 2001 before the beginning of the fiscal year on January 1.

Staff from the Finance Department and the other City departments stand ready to assist the Mayor, City Council and citizens in reviewing my Recommended 2002 Update Budget. I also want to express my appreciation to the many City staff members who worked diligently to develop solutions to address deficit issues in this budget that minimize the effects on services.

Respectfully,

John F. Shirey
City Manager